The impact of *Leegin* on the legislative systems' treatment of resale price maintenance cases

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Abstract

For decades, vertical restraints and especially resale price maintenance (RPM) have been considered anti-competitive in both Europe and the U.S.

However, the U.S. experienced a radical change in its antitrust policy, when the U.S. Supreme Court held in *Leegin Creative Leather Products, Inc. v. PSKS, Inc*. that RPM is subject to the rule of reason rather than per se illegal. Through the years, the change in the U.S. antitrust law has been affected by the development of economic theories, which led to today's approach in RPM. In contrast, there are debates in Europe about whether RPM should be deemed a hard-core restraint. Even after the policy change in the U.S. and the development in economic theories, in Europe RPM is still considered as anti-competitive under art. 101 (1) TFEU and can hardly be justified under art. 101 (3) of the treaty.

This thesis aims to investigate the impacts of *Leegin* on the European litigation systems' treatment of RPM cases. Alternatively, the thesis will consider whether the Court of Justice of the European Union (CJEU) should consider RPM on case-by-case basis rather than holding it to be per se illegal.

The research is based on an analysis of available European case law since 2007 in both the CJEU and the European Commission. Moreover, the thesis discusses the effects of RPM on the relevant market and consumer welfare based on economic theories and outweigh them with a legal perspective. The data has been collected through three different methods, literature review for legal and economic analysis, a questionnaire developed by the author, and in-depth interviews with several legal scholars.

Even though economists and legal scholars argue in favour of the positive effects of RPM on the market and advocate the court for a more flexible regime, the lack of empirical evidence and resources to perform real economic analysis leads the European litigation systems to presume that RPM is anti-competitive and should rarely be justified under art. 101 (3) TFEU.

Abbreviations

BEVR	Block Exemption on Vertical Restraints
CJEU	Court of Justice of the European Union
EC	European Commission regulation
EU	European Union
GC	General Court
RPM	Resale price maintenance
RRP	Recommended resale price
SME	Small and medium sized enterprise
TFEU	Treaty on the Functioning of the European Union
U.S.	United States of America
Vertical Guideline	Commission Guideline on Vertical Restraints

Content

1 Introduction

1.1 Background

For years, economists and lawyers have debated whether RPM should be considered a hard-core restraint because of its effect on the relevant market and consumer welfare. RPM is a resale price imposed by the manufacturer on its retailers; it can be a fixed, minimum or maximum price. While, the relevant market is a combination of a relevant product market and the relevant geographic market. Where a relevant product market means comprising all the product and services which are interchangeable and substitutable by the consumer, and a relevant geographic market means the undertakings concerned are involved in the supply and demand of goods and services.[1]

RPM did not get enough attention from the European litigation systems in the past decade. However, in 2018 the European Commission in 2018 held ASUS, Philips, Pioneer, and Denon & Marantz liable for the infringement of art 101 (1) TFEU as a consequence of imposing RPM on its retailers. The European Commission decision came as a reaction to the rapid development in e-commerce sales, where manufacturers started to use comparison websites and software programs to monitor their retailers' resale prices.[2]

Conversely, in 2007 the U.S. experienced a radical change in the treatment of RPM, when the U.S. Supreme Court overruled in *Leegin* a well-established precedent concerning the treatment of RPM as subject to a rule of reason rather than per se illegal. The change in the treatment of RPM in the U.S. is mainly affected by the continuous development of economic theories.

[1] Commission notice on the definition of relevant market for the purposes of Community Competition law (97/C 732/03) Text with EEA relevance 9.12.1997. Chap.II no. 7-9
[2] Commission, E. "Antitrust: Commission fines four consumer electronics manufacturers for fixing online resale prices" [2018] [Read 19.10.19].

1.2 Research question and aim of the study

This thesis raises two questions as a result of the aforementioned. First, did *Leegin* have an influence on the European litigation systems in their treatment of RPM cases? Or should European litigation systems treat the RPM cases on case-by-case- basis, taking into consideration the competition effects on the relevant market and consumer welfare?

The study aims to spotlight the importance of a multidisciplinary analysis of treating RPM in competition law cases.

The combination of the law and the economic approach could provide a vital instrument for the European Commission, in considering the effects of RPM on the competition in the relevant market and consumer welfare in the upcoming BEVR.

1.3 Methodology

In this thesis, the data has been collected by three different methods. The first, a literary review of legal and economic analyses; the second, a questionnaire developed by the author; and the third, in-depth interviews with several legal scholars.

1.3.1 Literature review

This study uses the legal instruments defined in the European Commission guidelines on vertical restraints, as well as economics and comparative methods. It consists of three separates but connected analyses that present the current framework of RPM in Europe. These are the prohibition of RPM under art. 101 (1) TFEU, the exemption under art. 101 (3) TFEU, and the regulation 330/10. The study then compares the current Framework of RPM in Europe to the American legal framework around RPM. The comparison is based on analysing different cases; hence, the development in the litigation system in Europe and the U.S. The discussion represents the economic theories and legal scholars' perspectives since the European case laws are vague when analysing the effects of RPM on the competition in the relevant market.

1.3.2 Questionnaire

The author has developed a questionnaire in order to measure the effect of RPM on different retailers/manufacturers. The questionnaire contains the following components:

1. What is your opinion on RPM as a retailer/manufacturer, and why?
2. How will RPM affect you as a firm, if the European Commission decided in their new guideline that the manufacturer can impose a resale price on its retailers?

The questionnaire was sent to 20 Norwegian retailers and manufacturers, nine of which have replied. Three of them provided relatively relevant answers.

1.3.3 In-depth interviews

The author has conducted seven in-depth interviews. Six of them were among employees in the Swedish Competition Authority, and one was with the Norwegian Swedish competition lawyer in Sweden. The interviews contained open questions in which the author asked about the following:

1. On average, how many RPM cases do you deal with every year?
2. Comparing the last two RPM cases (CEPSA and Pedro IV)[3] treated in the CJEU with the last two RPM decisions in Sweden (13:e protein Import AB and Ifö Sanitär AB)[4]. It gives the impression that the Swedish Competition Authority is considering RPM on a case-by-case basis. What do you think about that and why?
3. How will the change in the Commission's guideline on vertical restraints affect your treatment of RPM cases as a Competition Authority?
4. Did you notice an increase in the number of RPM cases, as a result of e-commerce?
5. What is your prediction about the future of RPM?

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[3] C-279/06, *CEPSA Estaciones de Servicio SA v LV Tobar e Hijos SL* ECLI:EU:C:2008:485; C-260/07 *Pedro IV Servicios SL v Total España SA* ECLI:EU:C:2009:215.

[4] Swedish Competition Authority decision 01.06.2018 in case Dnr 339/2015, *Ifö Sanitär AB*; Swedish Competition Authority decision 30.10.2014 in case Dnr 559/2013 *13:e Protein Import AB.*

2 Source of the law of RPM

This chapter will outline the legal framework of RPM. The law of RPM is based on both primary and secondary sources of law: the TFEU art. 101,[5] BEVR regulation 330/2010,[6] the European Commission Vertical Guideline and case law.[7]

First, the author will discuss the essential elements of the prohibition of art. 101 (1) TFEU and their relation to RPM. Thereafter, the legal exemptions mentioned in art. 101 (3) and BEVR will be considered. Finally, the treatment of RPM in Europe and the Sherman Act in the U.S. antitrust law will be briefly compared.

2.1 Art. 101 (1) TFEU

Art. 101(1) TFEU is applied to multilateral or bilateral conduct in the form of an agreement or concerted practice. RPM usually involves bilateral or multilateral agreements between a manufacturer and a retailer. Therefore, it is dealt with within the framework of art. 101(1) TFEU.

Although it may seem that art. 101(1) TFEU refers directly to RPM agreements, it is important to look more closely at the legal context of the prohibition. The article and the case law show that five essential elements must be considered for an agreement to fall within the scope of art. 101 (1).

First, The CJEU and the GC have clarified when prohibited agreements exist. For instance, in the Bundesverband der Arzneimittel-Importeure eV and Commission of the European Communities v Bayer AG (Bayer AG), the CJEU evaluated the parties' intentions, and clarified that tacit agreements should also fall under the prohibition art. 101 (1) TFEU.[8]

[5] Treaty on the Functioning of the European Union - Common rules on competition, taxation and approximation of laws art. 101 C.F.R. [2016].
[6] Council Regulation (EC) No 1/2003 of 16 December 2002 on the implementation of the rules on competition laid down in Articles 81 and 82 of the Treat, art. 2 C.F.R. [Hereinafter regulation 1/2003].
[7] Commission Notice on Guidelines on vertical restraints. Commission regulation no. 330/2010. Text with EEA relevance 20.04.2010. [Hereinafter commission Guideline].
[8] C-2/01P and C-3/01P *Bundesverband der Arzneimittel-Importeure eV and Commission of the European Communities v Bayer AG* ECLI:EU:C:2004:2, Para. 102.

Unilateral agreements are Usually exempted in BEVR, such as agency contracts. However, CEPSA Estaciones de Servicio SA v LV Tobar e Hijos SL (CEPSA) is an exemption example where, the CJEU held that an agency agreement that includes a clause on purchase exclusivity and fixed prices can fall within the scope of art. 101 (1) TFEU.[9]

Second, the RPM agreement must affect the free competition on the market and trade between the Member States. The European Commission expresses in the Vertical Guideline that a manufacturer or a retailer should not affect the trade between Member States, if its market share is below 15%. The European Commission also presumes that vertical agreements between SME undertakings rarely affect the trade between Member States. [10]

Third, the restricted conduct must restrict competition either directly or indirectly by its object or effect. To determine if an agreement restricts competition by its object, it must almost always lead to restriction of competition. The content of the clause must be evaluated in the relevant economic and legal context. If an agreement restricts competition by effect, the competition might have been restricted or there is a potential for restriction.

Fourth, if an agreement infringes art. 101 (1) TFEU, it must be annulled as stated in art. 101 (2) of TFEU. In *Établissements Consten S.à.R.L. and Grundig-Verkaufs-GmbH v Commission of the European Economic Community (Consten and Grundig)*, the CJEU held that the claUses that infringe art. 101 (1) TFEU are nullified, unless they are not separable from the agreement itself, in which event the whole agreement must be nullified.[11]

Fifth, the EU competition law approach to RPM is as restricted conduct by its object and is therefore considered a hard-core restraint, but it can be justified if it satisfies the four conditions in art. 101 (3) TFEU. Therefore, a relative analysis of both anti-competitive and pro-competitive effects of an RPM agreement is required.

2.2 Art. 101 (3) TFEU

Art. 101 (3) TFEU is based mainly on an economic evaluation of the evidence, where the European legislative systems determine whether the agreement leads to an improvement of

[9] C-279/06, *CEPSA Estaciones de Servicio SA v LV Tobar e Hijos SL* ECLI:EU:C:2008:485, para. 48.
[10] Commission Notice on Guidelines on vertical restraints. Commission regulation no. 330/2010. Text with EEA relevance 20.04.2010, Para. 8-9.
[11] *Établissements Consten S.à.R.L. and Grundig-Verkaufs-GmbH v Commission of the European Economic Community* ECLI:EU:C:1966:41, para 347-8.

competition in the market or technical/economic progress. The pro-competitive effects must outweigh the anti-competitive effects to be justified under art. 101 (3) TFEU. Therefore, the principle of proportionality must be applied. Moreover, the RPM agreement cannot eliminate a substantial part of the competition. According to the European Commission, the notifying party must prove the likelihood of "appreciable objective advantages", which can compensate for the disadvantages of the agreement.[12]

To summarise the above, there must be an appreciable objective advantage.

Secondly, the European Commission should analyse and determine whether the conduct decreases the efficiency and, if so, to what extent. Lastly, the gain in efficiency must be analysed from the consumer welfare perspective and the effect on interbrand and intrabrand competition. Interbrand competition is between a supplier and a retailer that has developed a brand for their products to distinguish them from other brands. Intrabrand competition is between retailers or distributors of the same brand. It may be on price or non-price terms.[13] In other words, the gain of efficiency must be greater than the loss of efficiency to be justified under art. 101 (3).

2.3 Regulation (EU) 330/2010

Regulation 330/2010 is known as the umbrella block exemption regulation for vertical agreements (BEVR). Vertical agreements are between operators from the upstream and downstream markets in the economic process.[14]

If an RPM agreement does not satisfy the criterion mentioned in art. 101 (3) TFEU, the restricted agreement can be justified by bringing the agreement in line with BEVR 330/2010.

According to the BEVR, some agreements are exempted from the regulation, because they "*can improve economic efficiency within a chain of production or distribution by facilitating*

[12] C-501/06 P, C-513/06 P, C-515/06 P and C-519/06 P, *GlaxoSmithKline Services Unlimited v Commission of the European Communities and Commission of the European Communities v GlaxoSmithKline Services Unlimited and European Association of Euro Pharmaceutical Companies (EAEPC) v Commission of the European Communities and Asociación de exportadores españoles de productos farmacéuticos (Aseprofar) v Commission of the European Communities* ECLI:EU:C:2009:610, Para. 90.
[13] Plooy, Hazel Du, "*A quick overview: Intra-brand competition vs inter-brand competition*" Dingley Marshall 2018. [read 20.10.2019]
[14] Wijckmans & Tuytschaever, *Vertical agreements in EU competition law* [2011], p. 50.

better coordination between the participating undertakings. In particular, they can lead to a reduction in the transaction and distribution costs of the parties and to an optimisation of their sales and investment levels."[15]

Art. 2 of the BEVR 330/2010 provides a safe harbour to some vertical agreements, if the supplier or buyer's market share does not exceed 30% of the relevant market according to art. 3. Another important exception of art. 2 is art. 4, which lists all hard-core agreements, including fixed or minimum RPM, but maximum RPM might benefit from BEVR if the market share of the supplier does not exceed 30%.

According to the European case law and the European Commission, RPM is considered a hard-core restriction.[16] For instance, in *SA Binon & Cie v SA Agence et messageries de la presse (Binon)*, the CJEU stated that "*provisions which fix the prices to be observed in contracts with the third parties constitute, of themselves, a restriction of competition within the meaning of [art. 101 (1)] which refers to agreements which fix selling prices as an example of an agreement prohibited by the treaty.*
In those circumstances, where an agreement which establishes a selective distribution system and which affects trade between member states includes such a provision, an exemption from the prohibition contained in [art. 101 (1) TFEU] may only be granted through a decision adopted by the Commission in the conditions laid down by [art. 101 (3) TFEU]".[17]

The passages above demonstrate that the European courts should consider the consequences or restrictions of RPM agreements to determine whether there is an actual or a likelihood of an anti-competitive effect on the relevant market. For instance, a court should consider the economic context in which the undertakings operate, the market power, and which agreements cover the goods and services.

[15] Commission Regulation (EU) No 330/2010 of 20 April 2010 on the application of Article 101(3) of the Treaty on the Functioning of the European Union to categories of vertical agreements and concerted practices, C.F.R. [2010], recital 6.
[16] Commission Regulation (EU) No 330/2010 of 20 April 2010 on the application of Article 101(3) of the Treaty on the Functioning of the European Union to categories of vertical agreements and concerted practices, C.F.R. [2010], art. 4 (a).
[17] C-243/83, *SA Binon & Cie v SA Agence et messageries de la presse* ECLI:EU:C:1985:284, para. 44-45.

2.4 U.S. antitrust law vs. European competition law approaches to RPM

In order to understand the development of RPM in the U.S., it is essential to look at how the U.S. antitrust law asses RPM and how its operation differs from the European competition law.

The relevant legislative framework for RPM is the Sherman Act, which introduced modern antitrust law in the U.S.[18] Since its roots come from the common law, the U.S. courts adopted several terms of the common law to interpret the Sherman Act, such as the per se rule and the rule of reason. The purpose of the Sherman Act is to federalise and make the common law more effective by applying statutory jurisdiction over more than one state. Congress left the interpretation for the courts rather than providing long and detailed legislation in both sections 1 and 2. Different economic theories and law have influenced court decisions in different eras. This will be discussed further in chapter 3.

Section 1 of the Sherman Act covers anti-collusion that restricts commerce or trade, while section 2 prohibits unlawful monopolisation. The prohibitions in sections 1 and 2 of the Sherman Act show that Congress wished to prevent the domination of big enterprises and protect small companies.

Like the TFEU, the Sherman Act does not contain any provision specifically for vertical restraints. Nevertheless, the Sherman Act has been applied to the vertical agreements by the U.S. Supreme Court. Two aspects must be proven to be prohibited under section 1; first, there must be a multilateral or bilateral conduct "agreement", and secondly, the conduct must restrict the trade or commerce. As stated in the Sherman Act, an agreement is unlawful if it restrains trade or commerce, this resembles the restriction in art. 101 (1) TFEU. Only agreements that are considered unreasonable are prohibited, therefore section 1 is similar to art. 101 (3) TFEU and allows proportionate of pro- and anti-competitive effects of certain restricted conduct.

Throughout history, the development in case law in the U.S. shows, that the Sherman Act's prohibition of vertical restraints and especially RPM evolves to meet the dynamics of economic conditions. This will be discussed more in detail in the next chapter. The rule of

[18] Act of 02.07.1890, The Sherman Antitrust Act, enrolled Acts and Resolutions of Congress, 1789-1992.

reason implements this approach, where the U.S. Supreme Court in *Leegin* had to show that anti-competitive effects outweigh the pro-competitive effects of an RPM conduct to infringe Sherman Act section 1. On the other hand, the European Commission has been reluctant to incorporate the concept of rule of reason used in the U.S., because art. 101 (3) TFEU provides the appropriate balancing of pro- and anti-competitive effects of a restrictive agreement. Additionally, the concept of rule of reason might divert art. 101 (3) TFEU from its purpose. The aim of art. 101 (3) of the treaty is to provide a legal framework for an economic determination of the restrictive conduct and not to allow political considerations to set the competition law aside.[19] The CJEU supports the European Commission's view, having held in Métropole Télévision that it is "*only in the precise framework of [art. 101 (1)] that the pro and anti-competitive aspects of restrictions may be weighed… [art. 101 (3)] of the treaty would lose much of its effectiveness if such an examination had to be carried out already under [art. 101(1) TFEU*]"[20]. In other words, the European way of outweighing the positive and negative effects of competition's restriction in the relevant market is based on economic reasoning, rather than the public policy concerns like the rule of reason that is used in the U.S.

[19] European Commission, *White Paper on Modernisation of the Rules Implementing Articles 85 and 86 of the EC Treaty: Commission Programme No 99/027*: Office for Official Publications of the European Communities (art.101 and 102 TFEU) [1999], para. 56-58.
[20] T-185/00, T-216/00, T-299/00 and T-300/00, *Métropole Télévision SA (M6), Antena 3 de Televisión, SA Gestevisión Telecinco, SA and SIC - Sociedade Independente de Comunicação, SA v Commission of the European Communities* ECLI:EU:T:2002:242, Para. 74.

3 RPM in the U.S.

The U.S. was one of the first countries to adopt the rule of reason in treating RPM and vertical restraint cases. Since 1911 and until 2007, RPM was considered per se illegal. In 2007, the U.S. Supreme Court overruled *Dr. Miles Medical Co. v. John D. Park & Sons Co. (Dr Miles)* in *Leegin* from per se illegal to rule of reason by implementing the pro-competitive and anti-competitive effects in *Leegin*.[21] In the *Dr Miles* case, the U.S. Supreme Court established that vertical RPM cases are per se illegal and without reasonable justification, because they are anti-competitive and harmful to consumer welfare.[22]

In this chapter, a brief explanation of the development of the U.S. legislation system will be provided. First, the author will outline the essential eras in the history of RPM in the U.S. and then an analysis of *Leegin* and the situation today.

3.1 The legislative system before *Leegin*

In this section, some of the social contexts of RPM and vertical restraints will be mentioned to provide a clearer picture of the development in the U.S. The development of the U.S. legislation system is divided into three stages/eras, as shown below.

<u>The First Era (1890 - 1930):</u>

During this period, the U.S. courts differentiated between common law and the Sherman Act. The Sherman Act at that time applied to all restraints, while common law prohibited some of the restraints, which established a new field in antitrust law.[23] The common law during this era applied to what is called "ancillary restraints", while the Sherman Act applied to "naked restraints". Naked restraints are agreements that are explicitly anti-competitive, because they fix prices without offering any benefits.[24] Ancillary restraints are restrictions on the parties to

[21] No. 06-480, *Leegin Creative Leather Products v. PSKS, Inc*., 551 U.S. 877 [2007] [Supreme Court of the United States]
[22] No. 72*, Dr. Miles Medical Co. v. John D. Park & Sons Co,* 220 U.S. 373 [1911] [Supreme Court of the United States].
[23] Foer, Albert A., & Lande, Robert H, "*The Evolution of United States Antitrust Law: The Past, Present, and (Possible) Future*" University of Baltimore of Law [1999] [read 14.10.19], p.3; Jedlickova, *Resale price maintenance and vertical territorial restrictions* [2016], p. 56-71.
[24]Hovenkamp, Herbert J. "The Rule of reason" University of Pennsylvania Law School [2018] [read 15.11.2019]

the agreement and are related to the proper functioning of the agreement.[25] This division of these restraints laid the basis for differentiation and the application of the rule of reason and the per se illegal. The per se rule is applied only to naked restraints. Therefore, in the *Dr Miles* case, the U.S. Supreme Court stated that the minimum RPM agreement between Dr Miles and his retailers was per se illegal, because such an agreement was against the public interest. The public interest is the most crucial factor in antitrust law. Thus, agreements are not allowed to restrict the interests of the individuals or the public in their own businesses. Therefore, the agreement with the retailers and distributors was illegal and without reasonable justification.[26]

Strict era (1940 – the beginning of 1970)

This period is known as the strict era because of the strict legal and policy approach to antitrust law and the boom of economic theories in the U.S. Two schools were formed at that time, the Harvard School Theory in the late 1930s and the Chicago School Theory in 1950.[27] The Harvard School Theory was based on the empirical studies that identified the imperfection of competition as ways that a firm tries to avoid competition rather than ways to compete more efficiently. Harvard School Theory was ended at the beginning of 1970. In contrast, the Chicago School Theory, which is used now, believes that economic efficiency is the antitrust goal and a result of a free market, even though it may have some negative effects on consumers.[28]

Free era (in the late 1970- 1990):

The Chicago School Theory influenced the antitrust policy during this period, which led the U.S. Supreme Court to implement more of the economic aspects in its treatment of competition cases. During this period, the Supreme Court heard few RPM cases, and most of them were found not to violate the Sherman Act, section 1, because of the lack of market power. The lack of market power makes it difficult to prove that such a restricted agreement

[25] Concurrences. Ancillary restraints Concurrances. Retrieved from https://www.concurrences.com/en/glossary/Ancillary-restraints
[26] No. 72, *Dr. Miles Medical Co. v. John D. Park & Sons Co,* 220 U.S. 373 [1911] [Supreme Court of the United States].
[27] Jedlickova, *Resale price maintenance and vertical territorial restrictions* [2016], p. 71-90; Sawyer, Laura Philips, "*U.S. Antitrust Law and Policy in Historical Perspective*" [2019] [Read 14.10.19] p. 4-22.
[28] Piraino Jr, Thomas A, "*Reconciling the Harvard and Chicago Schools: a new antitrust approach for the 21st century*" [2007] [Read 13.10.19] p.348.

may have any effect in restricting or distorting interbrand competition or competition as a whole in the relevant market.[29]

<u>The rule of reason era (at the end of 1990 – 2010)</u>

During this era, the use of per se illegality to vertical restraints was denied by the Supreme Court, and the rule of reason was first implemented in 1997 in *State Oil Co. v. Khan* (*Khan case*) on maximum RPM and then in 2007 in *Leegin* to the remaining forms of RPM agreements. This development can be due to the Chicago School Theory that introduced the rule of reason to vertical restraints.[30] The rule of reason will be explained further in section 3.2. Even though the rule of reason was presented in *Leegin*, many states in the U.S. refused to implement it, because it is more difficult to win a case under the rule of reason than if the agreement is per se illegal.[31]

The exciting thing about *Leegin* is that the Supreme Court explained the pro-competitive effects that may justify the Use of RPM, and its role in increasing interbrand competition and consumer welfare. Moreover, the comparison was conducted to illustrate the positive and the negative effects of RPM in the relevant market.

3.2 *Leegin* Creative Leather v PSKS

The rule of reason was first established for all the forms of RPM by the U.S. Supreme Court in *Leegin*. The Supreme Court stated in that case that the main reason for implementing per se illegality was that there was a high probability of unreasonably restricting competition and decreasing outputs.

[29] Jedlickova, *Resale price maintenance and vertical territorial restrictions* [2016], p. 90-116. Van Doorn, Fredrik, "*Resale price maintenance in EC competition law: The need for a standardised approach"* [2009] [Read 13.10.19], p. 44-55 ;Hazıroglu, Elif Cemre & Gökatalay, Semih, "*Minimum resale price maintenance in EU in the aftermath of the U.S. Leegin decision"* [2015] [Read 15.11.19] p.50.
[30] Jedlickova, *Resale price maintenance and vertical territorial restrictions* [2016], p. 116-124. Foer, Albert A., & Lande, Robert H, "*The Evolution of United States Antitrust Law: The Past, Present, and (Possible) Future*" University of Baltimore of Law [1999] [read 14.10.19], p.11 ; Sawyer, Laura Philips, "*U.S. Antitrust Law and Policy in Historical Perspective*" [2019] [Read 14.10.19], p.10.
[31] Mulcahy, James "*Resale Price Maintenance: What Happened To Leegin Ten Years Later?*" [2017] [Read 18.10.19].

In this section, the author will provide a brief summary of *Leegin*. Then, the Supreme Court judgment will be analysed to understand the elements applied to overrule the per se illegal and apply the rule of reason.

Leegin was a manufacturer, designer, and distributor of leather goods and accessories. The brand started selling women's belts and other products under the name Brighton in 1991. Leegin believed that smaller retailers were more suitable for its products, because it had a policy that was focused on in-store customer experience and a high level of customer satisfaction. In 1997, Leegin changed its policy by implementing minimum RPM and refused to sell to retailers who would sell below these given prices. Later in 2002, Leegin found that one of their retailers, PSKS, had sold the products of Brighton with a price reduced by 20 % from the imposed minimum resale price. PSKS argued that other retailers were doing the same thing and that, therefore, he was forced to drop his prices to compete in the market. When PSKS refused to increase its prices, Leegin terminated their contract. As a result, PSKS sued Leegin for violating the Sherman Act, section 1. At the District Court, Leegin claimed that it was acting unilaterally and based their argument on the Colgate doctrine, but the jury found the agreement illegal. Leegin appealed, arguing that the rule of reason should be applied to this agreement. The Colgate doctrine applies to a company that announces a price in advance and wants its product to be resold and refuses to deal with retailers and distributors who do not respect its prices.[32]

Both the District Court and the Court of Appeals applied the per se rule following the same path as in the *Dr Miles* case.[33] However, the Supreme Court overruled the per se rule with five to four dissenting. The majority started by criticizing a few aspects of the *Dr Miles* decision before providing a ground for overruling the *Dr Miles* per se rule. The Supreme Court also showed some vital elements for the application of the rule of reason in future RPM cases.

As mentioned above, the majority of the Supreme Court criticised some aspects of the *Dr Miles* case, one of which is the judges' economic knowledge in the *Dr Miles*. The Supreme Court determined that *Dr Miles'* economic arguments were missing a real economic analysis of RPM.[34] *Dr Miles* is from the first era, as shown above in section 3.1, which means that the

[32] Bona, Jarod "*The Colgate Doctrine and Other Alternatives to Resale-Price-Maintenance Agreements*" [2018] [Read 04.11.19].
[33] *Leegin creative leather products, INC. V. PSKS, INC. (No. 06-480)*. Justice Kennedy – Opinion of the Court, chap. I.
[34] *Leegin creative leather products, INC. V. PSKS, INC. (No. 06-480)*. Justice Kennedy – Opinion of the Court, chap. III.

court decisions were influenced by the common law that was based on a formalistic legal doctrine with regard to RPM. Moreover, the economic theories, such as transaction costs and marginalisation theories, were not adopted in the American antitrust law until the 1970s. Therefore, *Dr Miles* did not analyse the possible motivation for entering into such an agreement.

The Supreme Court stated later that RPM most likely has a pro-competitive effect, because RPM enhances consumer welfare efficiency and promotes interbrand competition. The Court Used economic literature to support its holding of justifying the Use of the rule of reason in RPM cases.[35]

The Court in *Leegin* recognised three principal pro-competitive justifications for overruling per se illegality.

First, the majority held that RPM solved the free-riding problem by preventing the retailers from undercutting prices and encouraged them to invest in providing quality services for their consumers.[36] The free-riding problem is an issue in economics, where an undertaking benefits gratuitously from other undertakings' efforts or investments on products.[37]

Second, the Court addressed the new entrant justification. The Court stated that RPM eases the entering of new companies to the relevant market. Thus, it increases interbrand-competition by decreasing intrabrand competition.[38]

Third, increasing interbrand competition would encourage retailers to invest in providing services. The Supreme Court maintained that RPM gives the consumer the chance to choose among brands with low prices with low service or high prices with high service.[39]

These pro-competitive theories upon which the Court based its decision work only when the: Competitors decide not to facilitate RPM, because imposing RPM will lead to a reduction in the competitive price of the goods. Even though RPM introduces services that are beneficial

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[35] *Leegin creative leather products, INC. V. PSKS, INC. (No. 06-480*). Justice Kennedy – Opinion of the Court, chap. III, A.
[36] Ibid note 35.
[37] Competition, D.-G. f. (Ed.) (2003) Glossary of terms Used in EU competition policy. Retrieved from https://op.europa.eu/en/publication-detail/-/publication/100e1bc8-cee3-4f65-9b30-e232ec3064d6
[38] *Leegin creative leather products, INC. V. PSKS, INC. (No. 06-480*). Justice Kennedy – Opinion of the Court, chap. III, B.
[39] *Leegin creative leather products, INC. V. PSKS, INC. (No. 06-480*). Justice Kennedy – Opinion of the Court, chap. III, C.

for consumers, at the same time, it restricts intrabrand price competition. Moreover, other competitors decide to innovate, introduce services or even reduce their prices to compete with the increased intrabrand non-price competition.

The dissenting justices of the Supreme Court criticized the majority's decision, because they did not consider how often the free-riding problem occurred in the market, when they argued that RPM prevents free-riding. They contended further that the majority forgot to point out how the benefits of RPM outweigh the potential harms. They also reminded the majority of the aim of the Sherman Act, which is to maintain a marketplace free for anti-competitive practices.[40]

It is well known among economists that free-riding occurs with complex or technical products. The majority based their position on two empirical studies from the 1970s and 1980s. The studies point out the essential attributes of sophisticated products are quality and information.[41] In this case, leather is considered a product of quality and therefore falls within this category. The majority failed, in this case, to balance these two studies with other exciting studies that show the negativity of RPM.

Even though the majority chose to focus on the pro-competitive effects of RPM rather than balancing them with the anti-competitive effects, they recognized that RPM might have harmful effects like an increase in the resale prices. The Supreme Court stated that the main reason for the existence of RPM is to obtain a monopoly in the relevant market, but it is unlikely in a market that lacks significant market power. The majority expressed later that their concern is to enhance inter-brand competition and not intra-brand competition.[42]

The Supreme Court acknowledged that RPM could lead to an increase in retail prices, but this will be justified if the pro-competitive effects on consumers outweigh the anti-competitive effects.

[40] *Leegin creative leather products, INC. V. PSKS, INC. (No. 06-480)*. Breyer, J. – Dissenting, chap. I.
[41] Jedlickova, Resale price maintenance and vertical territorial restrictions [2016], p. 129.
[42] Ibid note 35.

3.3 The influence of *Leegin* in the U.S.

Leegin did not provide much guidance on how the rule of reason should be applied in RPM cases. The Supreme Court stated that only some of the essential factors that should be considered when dealing with an RPM case, of which the scope of operation and the existence of an agreement are the most important.

Under the scope of operation, there are again three essential elements. First, with regard to the undertaking's market power, the supplier or retailer must have significant market power in order to concern the courts. Secondly, if vertical collusion and horizontal collusion are treated differently, the Supreme Court stated in *Leegin* that horizontal agreements are per se illegal, while vertical agreements can be considered under the rule of reason. Thirdly, the parties' motivation when implying RPM usually differs between retailers, consumers and manufacturers. Consumers prefer lower prices, while manufacturers want to reduce the cost of distribution and not overcompensate retailers, who are the only ones who benefit from high retail prices.

As noted above, the Court did not mention why the rule of reason should be applied to RPM cases. Professor Hovenkamp has also confirmed that it is challenging to apply the rule of reason in RPM cases, because the Supreme Court did not give much guidance, the economic understanding of RPM is sophisticated, and the Dr Miles doctrine is baggage.[43] Some states in the U.S. still do not accept the rule of reason in RPM cases.

The dissent in *Leegin* acknowledged the difficulties involved in applying economics to RPM cases and noted that the law differs from the economy. The dissent mentioned that it is highly costly, highly technical and time-consuming if the courts must determine whether an undertaking has market power.[44] Therefore, the American courts as administrative systems apply rules that are workable for all parties. The dissent justice went on to summarise the *Leegin*: "*The only safe prediction to make about today's decision is that it will likely raise the price of goods at retail and that it will create considerable legal turbulence as lower courts seek to develop workable principles*."[45]

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[43] Areeda, & Hovenkamp, *Supplement to Antitrust Law: An Analysis of Antitrust Principles and Their Application* [2009], p. 238-239.
[44] Ibid note 40.
[45] *Leegin creative leather products, INC. V. PSKS, INC. (No. 06-480)*. Breyer, J. – Dissenting, chap. II, B.

One year after *Leegin*, the Third Circuit of the Court of Appeal in the U.S. applied essential factors that were established in *Leegin* to determine whether there was a violation of section 1 of the Sherman Act in the *Toledo Mack Sales & Service, Inc. V. Mack Trucks, Inc* (*Mack Truck case*).[46] The Mack Truck company had significant power in the market of heavy trucks in the U.S. Each distributor was assigned to a territory and was authorized to sell trucks. If a potential customer contacted one of them giving their specifications and requirements for a product, the dealer distributed the information to Mack Trucks. Then, Mack Trucks gave a rebated price under the name "sales assistance". Sales assistance was calculated based on a range of factors, and it was offered only if the product concerned was sold within the dealer's territory. One of Mack Truck's dealers "Toledo" tried to lower prices for its customers to be able to compete with the other dealers of Mack Trucks. Mack Trucks and its dealers tried to prevent this conduct.

Toledo claimed that Mack Trucks and its dealers violated Sherman Act section 1 by engaging in a vertical agreement with their dealers and that Mack Trucks refused to sell to dealers who wanted to sell outside of their territories. Moreover, the dealers were engaged in a gentlemen's agreement not to compete on prices.

The Third Circuit of the Court of Appeal found that the vertical collusion on refusal to sell falls under the rule of reason by referring to *Leegin.* The Court held that Mack Trucks violated the Sherman Act section 1 by analysing Mack Truck’s motivation in refusing to sell and market power misuse. The rule of reason was applied here, although the purpose of vertical collusion is to assist with the facilitation of horizontal collusion. The Court asserted later that the horizontal agreement between retailers on fixed prices is per se illegal according to *Leegin* because the horizontal agreement is considered anti-competitive.

[46] No. 07-1811, *Toledo Mack Sales & Service, Inc. V. Mack Trucks, Inc.* [2008] [United States Court of Appeals, Third Circuit].

4 The law and economics of RPM in Europe

For years, legal scholars have discussed how *Leegin* will affect the European litigation system in dealing with RPM cases. In this section, an analysis of European cases since 2007 will be provided to determine if *Leegin* has influenced the European case law.

4.1 CEPSA SA v. LV Tobar e Hijos SL

The question in this case was whether the contract between CEPSA and Tobar on imposing a maximum resale price infringed art. 101 TFEU.

In 1996, Tobar entered into an agreement with CEPSA SA to buy exclusively from CEPSA motor vehicles, fuels and other petroleum products at retail prices where the supplier established the conditions. The contract period was ten years with a possibility of five-years extension. During the contract period, Tobar was prohibited from selling or promoting other competing products both within the station area and the surrounding area. In 2001, CEPSA sent a letter to Tobar to reduce its sale price of petroleum but without affecting CEPSA's receipts. Later in 2003, Tobar stopped obtaining supplies from CEPSA and covered up CEPSA's logo on the service station. After that, Tobar brought an action against CEPSA, claiming that the contract infringes art. 81 EC [now art. 101 TFEU], because CEPSA decided itself the resale price of the products.

The Provincial Court of Madrid held that the agreement should be annulled on the grounds that the contract is prohibitive [now art. 101 TFEU] and is not compatible with the Vertical Guideline no. 2790/1990 [now no. 330/2010]. CEPSA appealed this judgement.

The CJEU held first that the agreement between CEPSA and Tobar falls under [art. 101 (1) TFEU], only if the retailer is regarded as an independent undertaking. According to case law, the term “undertaking” is every entity that is engaged in economic activity, regardless of its legal status.

In this case, the CJEU analysed whether Tobar went in agreement with CEPSA as an independent undertaking by determining whether the agent bore the commercial and financial risks when selling goods and services to third parties. The CJEU left this analysis to the national court based on the functions of the CJEU and national courts. The national court must analyse the risks that are mentioned in the contract on a case-by-case basis where the real economic situation will be considered. After considering all aspects of the contract, the Court held that the relationship between CEPSA and Tobar is identical to an agent and principal relationship. The Advocate General Mengozzi criticised this by arguing that the CJEU should have explained the difference between using an agency contract in the upstream market and downstream market before explaining how to determine if an undertaking is an independent undertaking.[47]

The Court added that the obligations imposed on the operator to sell goods to third parties on the principal's behalf fall outside of the scope of [art. 101 (1) TFEU]. The European Commission specified in its guidelines on [art. 101 TFEU] that, if an agency contract holds an exclusivity and a non-competition clause, it must be considered to infringe [art. 101 TFEU], because the agent is in principal an economic operator, and the clauses in the contract are capable of restricting competition in the relevant market. Therefore [art. 101 (1) TFEU] applies to such agreements.[48]

After explaining when a company is considered an undertaking, the CJEU stated that "***the fixing of the retail price of those goods constitutes restrictions of competition*** *expressly provided in [art. 101 (1)(a) TFEU], which brings the agreement within the scope of the prohibition laid down in the provision to the extent to which* ***all the other conditions for the application of that provision satisfied****, namely that the agreement has* ***as its object or effect of restricting appreciably competition within common market and is capable of affecting trade between member states*** ".[49]

The passage above shows that the agreements between undertakings on the fixed retail prices of goods and services do not automatically fall within the scope of art. 101 (1) TFEU. Therefore, the courts must determine whether an agreement restricts competition by its object or effect in the relevant market or trade between Member States. According to the case law, to

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[47] Opinion of Mr Advocate General Mengozzi: C-279/06, *CEPSA Estaciones de Servicio SA v LV Tobar e Hijos SL* ECLI:EU:C:2008:485, European Court Reports 2008 I-06681, para. 30-33.
[48] C-217/05, *Confederación Española de Empresarios de Estaciones de Servicio v Compañía Española de Petróleos SA* ECLI:EU:C:2006:784, Para. 62-63. [My emphasis]
[49] C-279/06, *CEPSA Estaciones de Servicio SA v LV Tobar e Hijos SL* ECLI:EU:C:2008:485, para. 42. [My emphasis]

do that, some elements must be considered, as the economic situation in the relevant market, and whether the agreement satisfies the conditions provided by the BEVR. Giving a proper analysis is necessary for the court; therefore, the CJEU expressed in para. 43 in this case that the national court can go even further by comparing the current agreement with similar ones to determine if there is any form of restriction or distortion of the competition on the common market or trade between Member States. The effect of vertical restraint agreements can also be assessed in the economic and legal context in which an agreement occurs and may be combined with other agreements, to consider if there is an infringement of art. 101 (1) TFEU. In other words, the Court expressed the importance of giving a multidisciplinary analysis of the effects of an agreement on the competition in the relevant market. The agreement must restrict or distort competition to fall under art. 101 TFEU. On the other hand, the Court stated: "*According to [article 4(a) of Regulation 330/10], the exemption provided for in Article 2 thereof was not to apply to vertical agreements* ***which have as their object the 'restriction of the buyer's ability to determine its sale price, without prejudice to the possibility of the supplier's imposing a maximum sale price or recommending a sale price, provided*** *that they do not amount to a fixed or minimum sale price as a result of pressure from, or incentives offered by, any of the parties'*."[50]

The passage above expresses that the CJEU considers RPM to be conduct that restricts competition by its nature. Therefore, it should fall under the scope of art. 101 (1) TFEU only if the operator had to sell at a fixed price that is imposed by the supplier. This means that an agreement that contains a recommendation or a maximum resale price will be block-exempted.[51] Therefore, the CJEU asked the national court to ascertain whether the fixed retail price that Tobar determined was granted by CEPSA, taking into account the effect of all the clauses of the contract in their legal and economic context. The Advocate General Mengozzi suggests in this case that fixing the retail price of the fuel by CEPSA should be considered void due to the occurrence of unilateral conduct unless it justifies the conditions listed in art. 101 (3) TFEU. [52]

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[50] Ibid note 49, para. 69. [My emphasis]
[51] Whish & Bailey, *Competition law (ningth ed.)* [2018], p. 662, point c.
[52] Ibid note 47.

The European Commission contradicted the decision in *CEPSA*, arguing that RPM agreements must be considered a hardcore restraint and are unlikely to fulfil the conditions of art. 101 (3) TFEU.

Even though the CJEU mentioned that such agreements could be block- exempted under art. 101 (3), it seems that the Vertical Guideline art. 4 (a) outweigh the positive effects on the consumers and market. Therefore, the agreement was considered as a restriction on competition. It can be argued that, if a retailer is restricted to decide its prices, this will lead to indirect harm on competition, which shows that there is a high threshold for RPM agreements to be justified under art. 101 (3) of the treaty.

4.2 Pedro IV v. Total España SA[53]

Pedro IV, who runs a service station entered into four contracts with Total España, a supplier of petroleum-based products. The first contract gave Total the right to build on land owned by Pedro IV, and Pedro IV had the right to own the building after 20 years. The second contract was a renewable leasing contract, in which Total granted Pedro IV the right to operate and Use the service station one year at a time. The third contract was an exclusive supply agreement for fuel, in which Pedro IV undertook to run the service station. Total informed Pedro IV of the recommended retail prices, and it imposed a fixed price to resellers established in Barcelona, where the price was not to be higher than the average price imposed by Total's rivals who operate in Barcelona. Lastly, in the fourth contract, Total granted Pedro IV a mortgage loan as security in the amount of approximately € 180 300.

In 2004, Pedro IV brought an action to the Commercial Court to annul all four contracts that include clauses that are restricting competition.

All of the contracts between Pedro IV and Total raise the same question, which is whether these contracts are eligible to benefit from the application of the block exemption. Nevertheless, the author of this thesis will analyse only the court decision of the third contract, which is more relevant for this thesis.

The National Court asked in this case whether the CJEU could establish whether contractual provisions relating to resale prices by an exclusivity purchasing agreement falls under the

[53] C-260/07, *Pedro IV Servicios SL v Total España SA* ECLI:EU:C:2009:215.

scope of [art. 101 (1)(a) TFEU] and is incapable of benefiting from the application of the block exemption provided on the ground that such provisions are subject to restrict the reseller's freedom to fix the retail price of the goods.

The CJEU started replying to this question by stating that [art. 101 (1) (a)] prohibits " *all agreements between undertakings which may affect trade between Member States and which have as their object or effect the prevention, restriction or distortion of competition within the common market… directly or indirectly, fix purchase or selling prices."*[54]

In this case, Pedro IV entered into an exclusivity agreement with Total, the first clause of which determines the price of the fuel sold in the Pedro IV service stations in Barcelona, and second required Pedro IV to guarantee that the price would never exceed the average fixed price of Total's rivals on the market.

Art. 4 of the BEVR states that vertical agreements are exempted from the prohibition in art. 101 (1) TFEU, "*which, directly or indirectly, in isolation or in combination with other factors under the control of the parties, have as their object: the restriction of the buyer's ability to determine its sale price, without prejudice to the possibility of the supplier to impose a maximum sale price or recommend a sale price, provided that they do not amount to a fixed or minimum sale price as a result of pressure from, or incentives offered by, any of the parties;"*

The question here is whether Total imposed directly or indirectly a fixed resale price that restricted Pedro IV's freedom to determine his resale prices.

The CJEU stated like the *CEPSA case,*[55] that art. 351 TFEU clarifies the division of jurisdiction between the national courts and the CJEU. The National Court has more knowledge of this kind of dispute and has the abilities to ascertain if the agreement included a fixed/minimum retail price or a recommended/ maximum retail price, taking into account all of the contractual obligations in their commercial and legal context, and whether the conduct of the parties constitutes, in reality, a fixed/minimum resale price and not a recommended resale price. The Court clarified the national court's role and its freedom to examine whether it is possible for the retailer to reduce the given recommended price and determine if the recommended price is, in reality, fixed or concealed by indirect means. If the National Court

[54] Ibid note 53, para. 71. [My Emphasis].
[55] Ibid note 49, para. 67 and 71.

found that Total infringed art. 101 (1) TFEU by imposing fixed retail prices on Pedro IV, the agreement would be ineligible for the BEVR regulation 330/2010.

The CJEU found that the first clause of the third contract did not distort competition, because Total informed Pedro IV about the recommended resale price only to ensure a fair competition with other distributors in the area, which means that Pedro IV was free to set the prices higher or lower than the recommended resale price imposed by the supplier. While the second clause, Pedro IV had to guarantee that his prices would not exceed the average fixed price of Total's rivals with a significant presence in the market. The CJEU also found that this provision of the contract did not concern a resale price, because it was a transaction agreed to between the two undertakings who are the contract's parties.

Pedro IV claimed that Total indirectly imposed a fixed retail price. The CJEU stated in this manner that it was for the National Court to determine whether Pedro IV was in reality bound by the fixed resale price imposed by Total.

The CJEU explained further that, for a restricted agreement to fall within the scope of [art. 101 (1) (a) TFEU], all the conditions provided in the article should be met, and the agreement should restrict or distort competition in the market by its object or effect, or be capable of affecting trade between Member States. As mentioned in CEPSA, the effect of such agreements should be assessed in the economic and legal context in which the agreements occur and where they might be combined with other agreements to have a cumulative effect on the market.

The CJEU did not, in this case, determine whether the agreement can be justified by the conditions provided for in art. 101 (3) of the treaty, where they concentrated only on art. 4 (a) of BEVR; in contrast to the *CEPSA case*, in which the Court determined both the art. 4 (a) of the regulation and mentioned that the agreement could be justified if the conditions in art. 101 (3) TFEU are fulfilled. This gives a signal that the Court is emphasizing the retailers' freedom to decide the resale price more than the efficiency gain that RPM may cause, if the Court considered the economic benefits of an RPM agreement. As mentioned in the previous case, some may argue that, when an infringement falls under the scope of art. 4 (a), it will most likely harm consumer welfare indirectly.

4.3 Asus, Pioneer, Philips and Denon & Marantz v. EU Commission

In 2018, the European Commission fined four electronics manufacturers separately (Asus, Pioneer, Philips and Denon & Marantz) more than € 111 million for violating EU competition law by engaging in a fixed or minimum RPM agreements or concerted practices that restrict the retailers' ability to set their resale prices.[56]

The European Commission has relegated to the Council Regulation (EC) 1/2003 the ability to conduct open investigations, request information and fine manufacturers found to have infringed the competition rules.

Even though the European Commission fined the four manufacturers separately in different decisions, the author of this thesis will analyse the European Commission's decisions together, because the Commission followed the same procedure in all of them.

Asus, Pioneer Europe, Philips and Denon & Marantz[57]

All four companies had as their part of the strategy to keep their products' price stable at the RRP in several European countries. To accomplish this, they monitored their retailers' prices by using a comparison website or other sophisticated software programmes to identify the retailers who did not follow the RRP imposed. The company contacted these retailers and forced them to increase their prices to the RRP, and, if they refused, to be sanctioned.

The European Commission found that all four companies (ASUS, Pioneer, Philips and Denon & Marantz) engaged in a single or continuous infringement of art. 101 (1) TFEU, by implementing conduct that restricted the retailers' freedom to set their resale prices independently.

The Commission started by considering whether the companies were engaged in an agreement or concerted practice with their retailers, according to art. 101 (1) TFEU. The agreements or concerted practices were between one of the mentioned companies on the one

[56] Commission, E. "*Antitrust: Commission fines four consumer electronics manufacturers for fixing online resale prices*" [2018] [Read 19.10.19].
[57] Commission Decision of 24.04.2018 in case AT.40465 *ASUS.*; Commission Decision of 24.07.2018 in case AT.40469 *Denon & Marantz*; Commission Decision of 24.07.2018 in case AT.40182 *PIONEER*; Commission Decision of 24.07.2018 in AT.40181 *PHILIPS*.

hand, and the company's retailers on the other hand, where the purpose of their conduct was to limit the resale price competition between retailers.

The European Commission considered the same elements as in the cases mentioned above. They first had to determine whether the actions were isolated but, at the same time, were part of an overall plan, because their identical objectives could distort competition in the internal market and the trade between Member States.[58]

Later, the Commission had to determine the effects of an agreement or concerted practice in the market. According to case law, certain categories of conduct are harmful to the competition by their nature.[59] Consequently, RPM may be considered a collusive behaviour that will likely have a negative effect on the prices, quality, quantity and choices of goods and services in the market.[60] The Commission concluded that the four companies' conduct restricted competition both in the internal market and trade between Member States.

The European Commission then determined whether the conduct's positive effects outweigh the negative effects by applying both art. 4 (a) of the BEVR and art. 101 (3) TFEU. To determine if the conduct was exempted, they argued that the concerted practice of the four companies limited the retailers' freedom to decide their resale prices and, therefore, it could not be exempted under art. 4 (a) BEVR. In addition, the agreement did not meet the conditions for justification in art. 101 (3) TFEU, since they could not indicate whether the retailers provided a pre-sale service for their products or if the agreement prevented free-riding between retailers in online and offline channels.

The Commission focused only on their treatment of the case law perception on RPM on goods and services rather than providing a real economic analysis of the effect of RPM on the market. It can be challenging to provide a proper economic analysis of RPM in the market, because it is sophisticated, as Hovenkamp argued.[61] This was also confirmed in the survey that the author carried out, where Norgesgruppen AS (MENY and KIWI) mentioned that, to

[58] Commission Decision of 24.04.2018 in case AT.40465 *ASUS*, p. 16.
[59] C-67/13 P, *Groupement des cartes bancaires (CB) v European Commission* ECLI:EU:C:2014:2204, para. 49; C-286/13 *P, Dole Food Company, Inc. and Dole Fresh Fruit Europe v European Commission* ECLI:EU:C:2015:184, para. 113.
[60] C-67/13 P, *Groupement des cartes bancaires (CB) v European Commission* ECLI:EU:C:2014:2204, para. 51; C-286/13 P, *Dole Food Company, Inc. and Dole Fresh Fruit Europe v European Commission* ECLI:EU:C:2015:184, para. 115.
[61] Areeda, & Hovenkamp, Supplement to Antitrust Law: An Analysis of Antitrust Principles and Their Application [2009], p. 238-239.

give a proper answer, they needed to provide a proper economic analysis that they lacked at that point of time, which means that RPM's effects on the market are more complicated than the resources that the Commission or the court can provide in their treatment. Moreover, the burden of proof in Europe rests on the defendant.

To conclude, the European Commission still considers RPM to be hard-core restraints, and there is a high threshold to be justified under art. 101 (3) TFEU.

5 The pros and cons of RPM

According to the CJEU, the primary condition in analysing whether an agreement restricts competition is determined by considering the undertaking's market power.[62] If the undertaking that imposes RPM has significant market power, it will infringe art. 101 (1) TFEU by its object. This is supported in the BEVR. Nevertheless, the CJEU did not provide much guidance on how to analyse the economics of RPM, except in *GlaxoSmithKline case,* in which the CJEU stated that "*[art. 101 TFEU] aims to protect not only the interests of competitors but also the structure of the market and competition in such*".[63]

On the other hand, the European Commission mentioned in its guideline on art. 101 (3) TFEU that the legislation systems should envisage an analysis that reflects on consumer welfare, this means connecting the concept of competition restriction with the price and output effects of a specific restraint.

In this chapter, the economic theories around RPM will be explained to determine whether RPM restricts competition and reduces consumer welfare in the relevant market and whether RPM falls within the scope of art. 101 (1) TFEU.

5.1 Pros of RPM

In *Leegin,* the majority judges sought support in economics literature inter alia Amici Curiae 9's statement that there is a widespread consensus. among economists that RPM may promote interbrand competition and consumers, which are the primary purposes of competition law; to underline the positive effects of RPM on the market. They added that RPM could have pro-competitive effects and that, especially under a variety of market conditions, it will not likely have an anti-competitive effect.[64] On the other hand, there is a wide disagreement among economists on the positive effects of RPM on the market and consumer welfare, which will be

[62] C-501/06 P, C-513/06 P, C-515/06 P and C-519/06 P, *GlaxoSmithKline Services Unlimited v Commission of the European Communities and Commission of the European Communities v GlaxoSmithKline Services Unlimited and European Association of Euro Pharmaceutical Companies (EAEPC) v Commission of the European Communities and Asociación de exportadores españoles de productos farmacéuticos (Aseprofar) v Commission of the European Communities* ECLI:EU:C:2009:610, para 63

[63] Ibid note 62

[64] *Leegin creative leather products, INC. V. PSKS, INC.* (No. 06-480). Justice Kennedy – Opinion of the Court, chap. I.

clarified below by outlining the pro-competitive effects and the potential reduction of consumer welfare.

Enhancing interbrand competition

Bork argues that RPM can be an efficient pricing practice that benefits consumers. For instance, RPM can lead to a reduction in intrabrand competition and enhance the interbrand competition; in a manner that will increase consumer welfare.[65] To understand this claim, one should understand that consumer demand depends not only on the price of a product but on other non-price factors as well. By imposing RPM, the manufacturer guarantees its retailers a particular profit margin on each unit sold, which will encourage them to provide more efficient presale services. In other words, RPM enhances retailers' ability to compete in other forms than prices, such as the quality of the product and better customer service to attract more customers. Figure 1 below illustrates how this concept works:

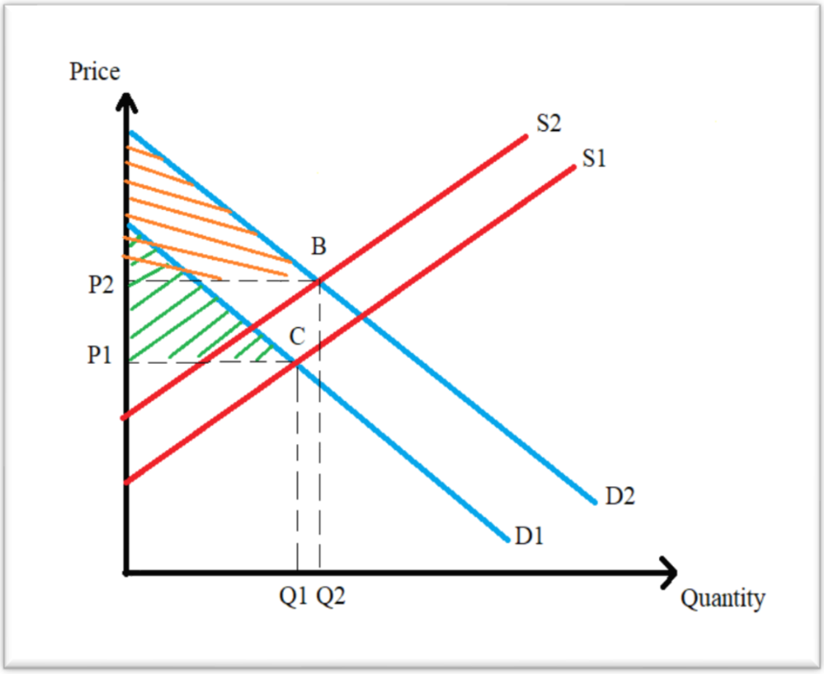

Figure 1 - RPM's effect on consumer welfare.
(Y-axis is price (P) and x-axis is the quantity (Q). D curves stands for the demand and S curves stands for the supply. The green shaded area is consumer surplus. before RPM and the orange shaded area is the consumer surplus. after RPM)

[65] Bork, *Antitrust Paradox* [1993], p. 198-201.

The pre-RPM equilibrium is at C (Q1, P1), where demand (D1) meets supply (S1). After enforcing RPM, the demand curve shifts outward in parallel from D1 to D2 because better services are assumed to increase the value of the products to all consumers. According to Bork, consumers will be willing to pay extra for the product, which means that the supply curve will move from S1 to S2. The new equilibrium point will be at B (Q2, P2). Under these conditions, the consumer welfare will increase because of RPM. As shown above, the orange shaded area is the consumer surplus after RPM and the green shaded area is consumer surplus before RPM.

Bork believes that consumer welfare is enhanced when allocative efficiencies, competition and wealth maximization are bundled up; economists disagree with him and argue that consumer surplus is the same as consumer welfare.[66] Consumer surplus is the difference between the price that consumers pay and the price that consumers are willing to pay.

Consumers are willing to pay extra for the product only if those extra services are provided. Bork concludes that RPM is highly pro-competitive and will enhance consumer welfare. Bork's economic theory assumes that consumers are interested in the non-price factors of the product, rather than the price of the products.[67]

The author of this thesis disagrees with Bork’s theory, as in reality, consumers can be price-sensitive, thus, the online shopping prove that consumers will opt for lower prices than pay a premium for instore for the same goods and services. This means that RPM does not always lead to an increase in the demand when the prices increase.

Preventing free-riding

Paldor and the majority judges in *Leegin* agree that RPM can prevent the free-riding problem on retailers who offer services,[68] which occurs mainly when a retailer benefits from other retailers' efforts on services. It usually occurs when a product (such as technical or complex products) needs pre- or post-sale services to consumers. Providing extra services will typically lead to an increase in the retail price.

[66] Ibid, note 65.
[67] Ibid note 65.
[68] Paldor, Itta, “*Vertical Restraints' Paradox: Justifying the Different Legal Treatment of Price and Non-Price Vertical Restraints*” [2007] [Read 13.10.19] p.17-20; *Leegin creative leather products, INC. V. PSKS, INC*. (No. 06-480). Justice Kennedy – Opinion of the Court, chap. III, A.

As shown in Figure 1, which is based on Bork's theory, an increase in price will lead to an increase in demand, since consumers are willing to pay extra for the services provided by retailers. The retailers are encouraged to invest in providing extra services to consumers, but they might lose their incentives, if non-services retailers are free-riding on their efforts. Free-riding occurs when non-services retailers Uses the fund derived by not supplying services to cutting prices in order to attract consumers. To protect the service-retailers, manufacturers will enforce RPM to stop non-service retailers from discounting, which means that retailers will not be able to compete in prices, but they can focus on other aspects, such as services. This theory is criticized by some legal scholars, such as Fournier, Lao and Grimes, who argue that the free-riding problem rarely occurs in the market and it may appear only in the market of complex or technical products that require pre- or post-sales.[69]

In the author's opinion, the price and the services provided are not the main factors that affect product demand. Geographic distance and accessibility may play an essential role in the consumers' choice. Even though consumers might prefer retailers who supply high-quality service, they might still go to the non-service store that is nearby. In short, the consumers are not necessarily attracted by the services provided, yet, accessibility, convenience and price level play an essential role in the consumer demand shifting.

Protecting brand image

Manufacturers may enforce RPM to protect their brand image of quality. Many manufacturers think that any reduction in the price of their products may reduce their sales volume, because high priced products signal consumers that the product is of quality and should be sold at prestigious outlets. In this case, some retailers may free ride on the quality certification offered by the prestigious stores. Therefore, the manufacturer imposes RPM to void competition in prices and guarantee prestigious retailers a plentiful margin in exchange for their high services.

[69] Gippini-Fournier, Eric, "*Resale Price Maintenance in the EU: In Statu Quo Ante Bellum?"* [2009] [Read 13.10.19] p. 9-12; Grimes, Warren, "*Resale price maintenance: a competitive assessment"* [2009] [Read 13.10.19], p. 27-30; Lao, Marina, "*Leegin and Resale Price Maintenance-A Model for Emulation or for Caution for the World*?" [2008] [Read 13.10.19], p. 253-258.

New manufacturers entry

It is not easy for new manufacturers to enter the market and promote their new products to distributors. Therefore, manufacturers choose to assure a high margin to distributors, to introduce their goods to the market. It is well known among economists that differentiation in the products for the same good in the relevant market, will increase consumer welfare because consumers will have a range of different alternatives available for them.

The issue here arises when distributors must take a risk in investing in promoting the new products. Later, if these investments are made, and the distributor starts to make some profit, the other distributors who did not take the risk will start to compete to gain some of the original distributor’s profit. Imposing RPM helps the distributors return on investment (ROI). Nevertheless, RPM prevents price competition which facilitate the market entry for the new manufacture. On the other hand, Fournier argues that the manufacturers’ goods will find their place on the shelves if they meet retailers’ criterion without using wealth transfer.[70]

The author disagrees with Fournier. The goods might find their place on the retailer’s shelves if they meet the retailer's criterion, and if the proper investment has been made at the right advertising channels. Thus, the retailer investment is still at risk for an entry product. The author believes that the manufacturer should consider sales support in such cases.

Demand uncertainty

According to Marvel and Peck, minimum or fixed RPM may reduce the risks that retailers take due to uncertain consumer demand of the products when they can decide how much of the goods to purchase from the manufacturer.[71] Demand uncertainty occurs when a retailer is unable to predict the consumer demand of the products to enable the retailer to keep an adequate level of inventory of the manufacturers' products.[72] RPM in these cases prevents retailers from discounting the prices of the products and sharing the risk with the manufacturer. Thereby, the retailer will make enough profit to cover the cost of buying an adequate level of inventory.

[70] Gippini-Fournier, Eric, “*Resale Price Maintenance in the EU: In Statu Quo Ante Bellum?”* [2009] [Read 13.10.19], p.13
[71] Deneckere, Raymond, Marvel, Howard P., & Peck, James, “*Demand uncertainty and price maintenance: Markdowns as destructive competition*” [1997] [Read 13.10.19], p. 619-641.
[72] Burch, Jan, “*What is demand uncertainty?”* [2018] [Read 12.10.19].

Double marginalization

Eliminating double marginalization is a well-known argument for imposing RPM in economic theories. It occurs when both the manufacturer and the retailers have specific market power and can maximize their prices above the marginal cost level to increase their profits. Ignoring the increase in price will lead to a reduction in the quantity of the products sold in the market. By imposing maximum RPM, the manufacturer will be able to adjust retail pricing to avoid the potential profit-loss related to the double marginalization, which will lead to improving economic efficiency and enhancing consumer welfare, because RPM prevents uncoordinated exercises of market power that exist at the upstream and downstream market.

5.2 Cons of RPM

Price increase

Fournier believes that RPM will lead to an increase in price,[73] which may in turn lead to a decrease in the quantity of demand. The author of this thesis drew figure 2 below, to illustrate this concept, where the demand will decrease from Q1 to Q2 when the price increases because of RPM from P1 to P2. The decrease in demand can occur, because some consumers may stop buying the products and may shift to other competing goods for a lower price, while others may keep buying the products and be harmed because of the price increase, which means that any increase in the price of a good as a result of RPM may lead to a reduction in consumer welfare.

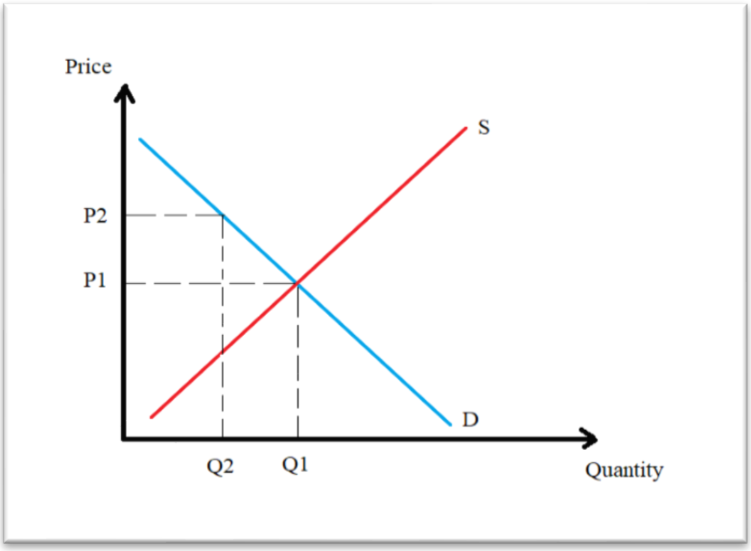

Figure 2 – RPM's effect on the demand
(X-axis is the Quantity and Y-axis is the Price. D stands for demand and S stands for supply)

Facilitating manufacturer cartel

Enforcing RPM can be Used by a manufacturer as a facilitating device. This effect is recognised by the European Commission and mentioned in its Vertical Guideline.[74]

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[73] Gippini-Fournier, Eric, "*Resale Price Maintenance in the EU: In Statu Quo Ante Bellum?"* [2009] [Read 13.10.19], p. 5.
[74] Commission Notice on Guidelines on vertical restraints. Commission regulation no. 330/2010. Text with EEA relevance 20.04.2010, para. 116 no.6.

It is easier for the manufacturer to observe and monitor resale prices than wholesale prices. However, the manufacturers will still sell at wholesale prices. If the manufacturers form a cartel, they will be able to find the retailers who cheat on the wholesale prices. Cheating means that the retailers will lower the price of the products to the end-Users, which will increase the demand and will thereby lead to a higher profit margin for retailers. Therefore, by imposing RPM, the manufacturer will be able to detect the retailers and hinder cheating more efficiently.

Facilitating a retailer cartel

The European Commission has also recognized the retailer cartel in its Vertical Guideline.[75] Manufacturers can enforce RPM not only as an easing device among them but also as facilitating device among retailers. In this case, imposing RPM will enable the manufacturer to easily recognise the retailer that sells at discounted prices and not only the ones who are selling at fixed prices.

Paldor argues that the common supplier will thereby find and punish the cheating retailer by withholding supplies.[76] In other words, the supplier will play the policing role at the retail level.

For a retailer to convince a manufacturer to impose RPM to sustain the retailers' cartel, the retailer must have absolute market power in the relevant market.

Foreclosing competition

Manufacturers with relatively high market share may impose RPM to motivate their retailers to deny the entry of other competitors.[77] The unavailability of alternatives, especially of unidentical products, may cause a loss in consumer welfare and hinder the achievement of Pareto optimality. Pareto optimality occurs when resources cannot be reallocated to make one individual better off without making the other worse off. [78]

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[75] Commission Notice on Guidelines on vertical restraints. Commission regulation no. 330/2010. Text with EEA relevance 20.04.2010, para. 128.
[76] Paldor, Itta, "*Vertical Restraints' Paradox: Justifying the Different Legal Treatment of Price and Non-Price Vertical Restraints*" [2007] [Read 13.10.19], p.11.
[77] Lamber, Thomas A., "*Dr. Miles is Dead-Now What: Structuring a Rule of Reason for Evaluating Minimum Resale Price Maintenance*" [2008] [Read 13.10.19], p.1945.
[78] CHAPPELOW, Jim, "*Pareto Efficiency*" [2019] [Read 12.10.19].

Manufacturers should have significant market power to convince retailers to deny other goods from entering the market.

Softening competition among retailers

Retailers may ask the manufacturer to impose RPM to soften competition between them. By imposing RPM, the new retailer cannot reduce its prices to attract more consumers. The duration of imposing RPM will affect the shape of the market structure and eventually will distort competition in the market, since all retailers will sell at the same price.

According to one of the retailers who replied to the questionnaire, RPM can cause harm to the retailers by limiting their abilities to compete in the relevant market.

Commitment problem

If a manufacturer commits to a distributor to distribute his products, the manufacturer eventually breaches this agreement if they do sell to other distributors at a lower price, to help them increase their market share and monopoly profit. By imposing RPM, the manufacturer cannot commit to its natural movement on lowering the wholesale prices to the new retailers, since it will not benefit the manufacturer, because the new retailer cannot sell at a discounted price. There the manufacturer will thereby earn a monopoly profit and not a competitive profit, which will harm consumer welfare.[79]

Damping system competition

Damping manufacturer competition and risking a high retail price will occur in a market in which duopoly retailers carry products of the duopoly manufacturers in a bargaining framework. Imposing RPM in this scenario will cause retailers to lose their incentives to negotiate on the wholesale prices by preventing the downstream from undercutting prices.[80]

[79] Van Doorn, Fredrik, "*Resale price maintenance in EC competition law: The need for a standardised approach"* [2009] [Read 13.10.19], p.72.
[80] Bennett, Matthew, Fletcher, Amelia, Giovannetti, Emanuele, & Stallibrass, David, «*Resale price maintenance: Explaining the controversy, and small steps towards a more nuanced policy*" [2009] [Read 13.10.19], p. 1289 - 1290.

5.3 Conclusion

The discussion above showed that the pro-competitive effect and anti-competitive effect of RPM depends on the conditions of the relevant market. Moreover, there is a broad consensus among economists and legal scholars that RPM cannot restrict or distort competition if the manufacturer does not have significant market power in the relevant market. RPM also has positive effects on the market by preventing the free-riding problem and improving the services provided to consumers.

Because of the lack of empirical evidence on the effects of RPM in the earlier cases, the frequency and significance of the pros and cons are mainly unknown and difficult to predict. Most of the pro-competitive effects of RPM are asserted from economic theories. Despite being recognised as credible among economists, the effects of RPM fail to constitute reliable evidence in court that contributes to the vindication of RPM. Moreover, most of the limited empirical evidence on RPM cases points out its anti-competitive effects, which makes people believe that RPM is more likely to be anti-competitive than pro-competitive.

6 The burden of proof

As shown in the case law in chapter 4, RPM is considered a hardcore restraint and has the same status. as per se illegal, which means that it restricts competition by its object. Therefore, the manufacturers are always asked to bear the burden of proving that RPM enhances efficiency and improves consumer welfare.

Art. 2 of the regulation 1/2003 and settled case-law provide that the burden of proof of an infringement of art. 101 (1) TFEU shall rest on the party or the authority alleging the infringement.[81] The defendant shall bear the burden of proof to fulfil art. 101 (3) TFEU conditions. In other words, the defendant must prove that RPM creates efficiencies and increase consumer welfare. The defendant must also prove that using RPM is the least restrictive way to achieve efficiencies and that it does not distort competition.

In practice, the defendants have to show the European Commission that RPM increased efficiency and improved consumer welfare. Mainly, the defendants managed to show that they met the first condition by referring to an economic analysis, but they failed to convince the European Commission that they met the second condition, which is improving consumer welfare, because, generally, the only information available is the price and the output before and after imposing RPM. This information is still not satisfying, as it is considered as RPMs' objectives.

The competition enforcement' presume that RPM has a negative impact on consumer welfare, which caUses implication when allocating the burden of proof. Therefore, the party who claims the positive effect of RPM will find it worthwhile to prove the welfare effects. Saying that, it can be difficult to meet the cumulative conditions of art. 101 (3) TFEU.

[81] Council Regulation (EC) No 1/2003 of 16 December 2002 on the implementation of the rules on competition laid down in Articles 81 and 82 of the Treaty, art. 2 C.F.R. [2003].

7 Prediction of the future

As shown above, the CJEU considers RPM a hard-core restraint because of its negative effect on the relevant market. Even though the CJEU cases are almost ten years old, and, in the meantime, economic development and an increase in the e-commerce market have occurred, the European Commission is still adopting the same opinion of the case law. This can be seen in the report on E-commerce sector inquiry, where the Commission states that RPM is determined as conduct that restricts competition by its object according to art. 101 (1) TFEU and a hard-core restriction according to art. 4 (a) BEVR.[82]

On the other hand, in most of the respondents' letters to the European Commission evaluating the BEVR show that the respondents are more open to the idea of implementing RPM, where some argued that RPM is known for its anti-competitive effects. However, it also has important pro-competitive effects, such as preventing the free-riding problem, which is a consequence of the online retailer's strategy. RPM helps to keep an adequate level of services and protect the retailers' margin level and the brand positioning in the relevant market. Moreover, they argued that RPM could be easily justified under art. 101 (3), if the Commission and the CJEU are more flexible in recognizing the potential positive effects of RPM. They concluded with a recommendation that the Commission should revise the current rules on RPM as a result of the increase in the Use of software programmes to monitor the prices in the market. Moreover, the consensus among economists on the positive effects of the RPM, supports the suggestion of revising the current framework around RPM.[83]

Moreover, some national competition authorities such as the Swedish competition authority started to consider RPM cases by weighing the positive and negative effects of RPM on the relevant market. This can be seen in both the *Ifö Sanitar case* and *13:e Protein Import AB case*, in which the Swedish Competition Authority considered the market share of the firms, alternative products available in the market for the consumers and whether there is a negative

[82] European Commission, "*Final report on the E-commerce Sector Inquiry*" [2017] [Read 21.10.19], para. 30
[83] European Commission, "*Factual summary of the contributions received in the context of the open public consultation on the evaluation of the Vertical Block Exemption Regulation (EU) No 330/2010*." [2019] [Read 21.10.19], p. 16; European Commission, "EU competition rules on vertical agreements – evaluation" [2019] [Read 22.10.19].

effect that outweighs the positive effect if an RPM is imposed, before finding that neither firm infringed art. 101 (1) TFEU.[84]

[84] Swedish Competition Authority decision 01.06.2018 in case Dnr 339/2015, *Ifö Sanitär AB*; Swedish Competition Authority decision 30.10.2014 in case Dnr 559/2013 *13:e Protein Import AB*.

8 Conclusion

This thesis attempted to answer, whether *Leegin* has an influence on the European litigation systems in its treatment of RPM cases, or whether European litigation systems should treat the RPM cases on a case-by-case- basis, taking into consideration the competition effects on the relevant market and consumer welfare.

By analysing the few cases that have been treated by the CJEU and European Commission in the past decade, the author of this thesis believes that the CJEU and the European Commission still have doubts with regard to the beneficial effects of RPM on consumers and competition in the relevant market. In short, *Leegin* did not have any impact on the European litigation system's treatment of RPM cases.

RPM is still determined a hard-core restraint under art. 101 (1) TFEU, even though art. 101 (3) of the treaty is open to a justification of the restricted conduct, if it fulfils all four conditions. According to the cases mentioned earlier in this thesis, it seems that the CJEU and the European Commission are emphasising the retailers' freedom to decide their resale prices more than the efficiency that RPM might gain. Therefore, the author believes that the CJEU and the European Commission are convinced that consumer welfare might be indirectly damaged by the restriction of the retailers' freedom to decide its resale price caused by imposing RPM. Secondly, the courts lack the resources required to perform an economic analysis of the effect of RPM on competition, as a result of which the CJEU's perspective remains the same.

The future of RPM in Europe is still uncertain, since there is much debate on the positive and negative effects of RPM on consumer welfare and competition in the relevant market. In the guideline's evaluation consultation held by the European Commission, several respondents recommended that the Commission should consider RPM on case-by-case basis instead of per se illegal. This means that, regardless of the rigid perspective of the CJEU and the European Commission on RPM, many national competition authorities, firms, and economists view RPM favourably.

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10 Attachments

10.1 Questionnaire

Questionnaire

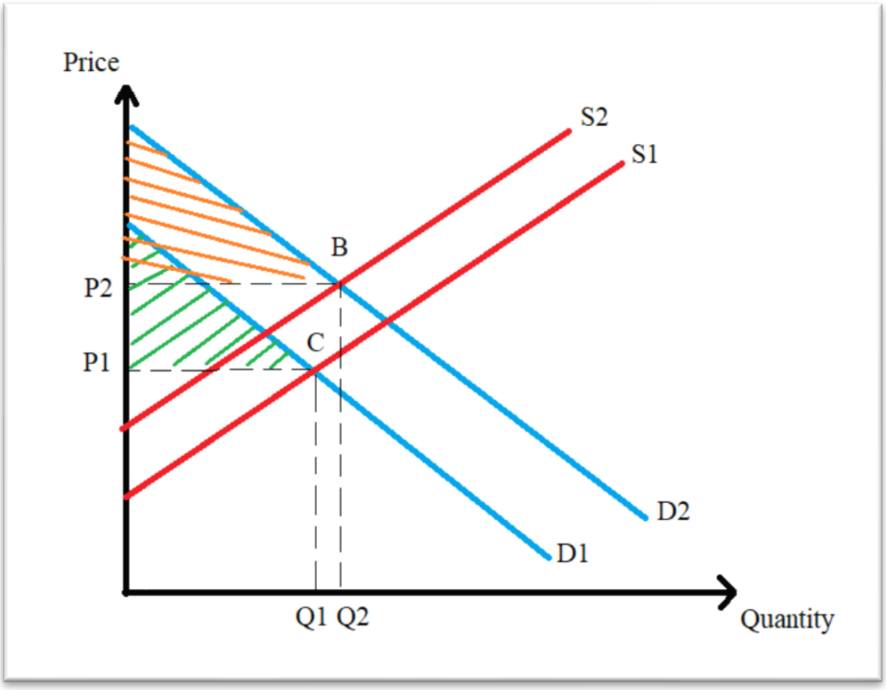
1. What is your opinion on RPM as a retailer/manufacturer, and why?
2. How will RPM affect you as a firm, if the European Commission decided in their new guideline that the manufacturer can impose a resale price on its retailers?

10.2 In-depth interviews

In-depth interviews

1. In average, how many RPM cases do you deal with every year?
2. Comparing the last two RPM cases (CEPSA and Pedro IV)[1] treated in the CJEU with the last two RPM decisions in Sweden (13:e protein Import AB and Ifö Sanitär AB). It gives the impression that the Swedish Competition Authority is considering RPM on a case-by-case basis. What do you think about that and why?
3. How will the change in the Commission guideline on vertical restraints affect your treatment of RPM cases as a Competition Authority?
4. Did you notice an increase in the number of RPM cases, as a result of the e-commerce?
5. What is your prediction about the future of RPM?

10.3 Figure 1 – RPM's effect on consumer welfare



10.4 Figure 2 – RPM's effect on demand